THE DIRECTOR OF
CENTRAL INTELLIGENCE

National Intelligence Officers

24 November 1981

NOTE FOR: Thomas Shoesmith
Deputy Assistant Secretary for
East Asia and Pacific

FROM : [redacted]
Assistant NIO for East Asia

STAT

SUBJECT : US-PRC Economic Relations

Attached are papers on this Subject -- past, present, and future.

Please let me know if anything else is required.

[redacted]

STAT

Attachment
As Stated

NFAC 7584-81

NATIONAL FOREIGN ASSESSMENT CENTER

WASHINGTON, D. C. 20505

23 November 1981

NOTE FOR: [redacted] STAT
Assistant NIO/EA

The material in this package does not directly address the question asked by Shoesmith, but it does give some insight into the US-PRC economic ties. The memo we plan to do will be much more useful because it will identify the specific areas that would be affected if economic ties were cut back due to a change in our political relationship with China.

[redacted] STAT

Richard J. Kerr
Director
East Asian Analysis

Approved For Release 2008/07/21 : CIA-RDP83B00551R000200050004-9

MEMORANDUM FOR: Deputy NIO East Asia

THROUGH: ~~D/CE~~, D/OEA

FROM: [redacted] CE/T STAT

SUBJECT: Materials on US-PRC Economic Relations

Attached are several pieces on US China economic relations requested by NIO EA's office. None of the items, dating back to the Blumenthal briefings, deal with the subject of the economic effects of a cutback in relations. This branch, however, is planning a research paper focussing on the relative economic importance to the US and China of the major items in US-PRC trade. The paper will look at the market shares of the major items and alternative markets and sources of supply for these goods. Particular emphasis will be placed on US exports of grain and the huge potential deals in oil exploration and drilling. Currently we are aiming at a mid to late~~r~~ December completion date.

[redacted] STAT

Acting Chief
CE/T

[illegible] BRIEFING
OCT 81

US-China Economic Relations

Since the establishment of diplomatic relations in 1979 US-China economic relations have burgeoned. Two-way trade has quintupled to $4.8 billion in 1980 from the 1978 level the United States has become firmly entrenched as the PRC's number three trading partner. With formal ties many obstacles to trade were removed -- the claims and assets problem was settled, a trade agreement granting reciprocal most favored-nation status was signed, and several bilateral economic agreements including textiles, shipping, and civil aviation were negotiated. In addition, China has become eligible for US Export-Import (EX-IM) Bank financing and Overseas Private Investment Corporation insurance on US investments in China. The first EX-IM credit agreement with the PRC was signed in October 1981 for a $28.4 million credit. Financial ties with US banks have also grown rapidly and several credit lines have been extended.

Progress in trade relations has also brought some problems. Beijing has expressed concern over its growing trade deficit with the United States and has been critical of US import restrictions particularly on textiles, China's economic readjustment has led to some cancellations of US equipment contracts and has clouded prospects for future sales. The large agricultural component in US exports, however, should help sustain current trade levels. 25X1

Recent Trends in Bilateral Trade

Although the overall increase in US-China trade has been rapid, the growth of China's imports have been especially dramatic. Purchases from the US rose from $1.7 billion in 1979 to nearly $3.6 billion last year. The increase, which came at the same time that a shift in China's domestic investment priorities slashed China's imports from Western Europe by almost 14 percent, moved the US firmly into position as China's second largest source of imports, just behind Japan and well ahead of West Germany. The Japanese and West German shares of China's total imports have eroded over the past few years while the US share has risen sharply from 8 percent in 1978 to 12 percent in 1979 and 19 percent last year. 25X1

Agricultural commodities accounted for 60 percent of imports from the US in 1980. Prior to 1978 Beijing treated the United States as a residual supplier of basic commodities such as grain, cotton, and soybeans, buying only for short-term exigencies. By 1980, however, the US was providing more than one-half of China's annual agricultural import needs. Other US exports which rose sharply in 1980 include wood and paper products -- much of which went to meet China's growing packaging needs -- as well as chemicals and synthetic fiber. 25X1

US exporters of machinery and equipment continued to be disappointed by the China market. In 1978, US firms watched from the sidelines as China signed contracts for more than $7 billion

This memorandum was prepared by China External Division of the Office of East Asian Affairs, National Foreign Assessment Center.

in Western equipment and technology. The inexperience of US firms in the China market, their inability to offer competitive financing because of the unsettled claims and assets issue, and the lack of normal diplomatic relations all contributed to the US capturing less than 1 percent of the 1978 orders. 25X1

Counters to the removal of many of the obstacles to US-China trade in 1979, Beijing instituted new investment priorities aimed at curbing a growing budget deficit and at reducing inflation. The shift in emphasis away from heavy industry toward light industry and agriculture resulted in severely curtailed plans for major equipment imports and halted the bulk of ongoing whole plant negotiations with most Western firms. 25X1

Further investment cutbacks in 1980 led to more cancellations or postponements of prospective deals including:

- An aircraft coproduction agreement and an accompanying jet engine deal valued at $1.9 billion.
- A broadcast and communications satellite system costing $250 million.
- An air traffic control system valued at $130 million.
- An agreement to provide equipment and to train personnel for the proposed Beijing High Energy Acceleration Center at an estimated cost of $100 million.

As a result of the cutbacks many US companies that scrambled for office space in Beijing during 1978-1979 period began cutting back their operations last year. 25X1

US machinery and equipment deliveries to China in 1980 amounted to only $350 million. Delivery of three Boeing 747SP aircraft worth $155 million accounted for all the growth as other machinery and equipment imports from the US fell 15 percent from the 1979 level. By comparision, machinery and equipment imports from Japan in 1980 were nearly 3 times those of 1979 at $1.6 billion, mostly on the strength of orders placed in 1978. 25X1

On the export side, Chinese sales to the United States in 1980 surpassed $1 billion for the first time. Textile exports were up 78 percent and accounted for nearly 35 percent of total sales. Even after the 1980 increase, however, textile sales to the United States continued to fall short of China's imports of US textile fibers. Crude oil and petroleum products, up 40 percent from the 1979 level, were China's second largest commodity export to the United States. While the bulk of China's 1979 oil sales to the US market were crude, refined products made up almost all of last year's $135 million in exports. 25X1

Despite the sharp increases over the past two years, sales to the US continue to account for only about 5 percent of China's total exports. The United States is China's third largest export market, well behind Japan and Hong Kong which together accounted for 43 percent ot total exports and just ahead of West Germany which took nearly 4 percent of China's 1980 exports. 25X1

Problems and Prospects for Future US-China Trade

The steady pattern of growth in US-China trade was broken in second quarter 1981 when US exports plunged almost 43 percent from the $1.2 billion peak first quarter level. With the steady advance in US imports the US surplus fell from $808 million in the first quarter to only $196 million in the second. About 80 percent of the second quarter export drop was due to lower US deliveries of wheat and cotton. High US cotton prices and good Chinese harvests for both commodities in 1980 probably caused the major impact on US sales. China's imports of US cotton in first half 1981 were less than one-third the record level for the same period last year.

While the overall growth of US-China economic relations has been viewed favorably by the Chinese, Beijing has continued to express its displeasure with certain aspects of several bilateral agreements and has pressed for improved terms of trade:

- Chinese trade officials have continued to voice their concern over the growing trade deficit with the United States. 25X1

- Textile negotiations have been among the most contentious in the relationship. The Chinese feel unduly constrained by the agreed upon textile quotas and have often argued that the quotas should be raised in view of the substantially greater amounts of raw cotton and synthetic fiber China imports from the US, as well as to aid in balancing trade. 25X1

- Eximbank's relatively high interest rate has discouraged extensive Chinese utilization of this credit which the Chinese have termed "uncompetitive". The Bank of China particularly was troubled by the Eximbank's legal requirement that any loan offered to it must be guaranteed by the full faith and credit of the People's Republic. 25X1

- Beijing remains interested in receiving preferential treatment under the General System of Preferences (GSP). China's membership in the International Monetary Fund (IMF) and its most favored nation trade status leave only its accession to the General Agreement on Tariffs and Trade (GATT) as the remaining requirement under US law before China can be considered for GSP. However, the Chinese recently suggested to a visiting congressional delegation that the law be changed to eliminate this requirement. 25X1

- During maritime negotiations held in September, the Chinese pressed for additional port access and relaxed visa requirements, although differences over cargo sharing dominated the talks. [redacted] 25X1

- The refusal of Chinese civil aviation authorities to permit Pan American to begin flying a third frequency into China as stipulated in the civil aviation agreement highlights Beijing's continuing concern that its own air service is not competitive with foreign carriers. The issue was temporarily resolved over the summer by Beijing's willingness to allow Pan American to fly third frequency as an "extra section". [redacted] 25X1

Although the growth of US exports to China will probably slow this year the overall prospects for US-China trade remain good. Imports to China will continue, however, to be dominated by agricultural goods. The US-PRC grain agreement concluded in October 1980 provides for annual purchase of 6 to 9 million tons of wheat and corn during the 1981-1984 period. Although the Chinese were given permission to purchase more grain than allowed in the long term agreement (LTA), sales this year will be slightly less than last year's record 8 million ton level probably be due to China's good domestic harvest. [redacted] 25X1

Despite the more drastic drop in purchases the US will continue to be China's major supplier of cotton to support Beijing's efforts to improve living standards and its increased emphasis on textile exports. With domestic investment in petrochemicals being scaled-back, US prospects for synthetic fiber exports also remain good. Other areas where the US may continue to make inroads include wood and pulp, fertilizers, and chemical products. [redacted] 25X1

In heavy industry China's new investment priorities will hold contract signings at depressed levels over the next few years. Most of the contracts with firms remain unsettled. The affected US contracts were almost entirely for technology associated with petrochemical plants sold by Japanese, West German, and UK companies. Payments under these sub-contracts will probably take place only when the major suppliers receive final payment. [redacted] 25X1

25X1

While major plant and equipment purchases will lag in the near term US firms will still be major competitors for sales of oil exploration, hydropower, communications and transport equipment, items still actively sought by Beijing. [redacted] 25X1

The expected narrowing of the bilateral deficit this year may ease Beijing's concern over this issue in the short-run but long-run interest in boosting sales to the lucrative US market will remain. Efforts underway by China to expand exports of light industrial goods will continue to encounter resistance whenever these goods infringe on domestic markets. Although the Chinese have been more vocal in complaints over the trade deficit with the United States now nearly three times the PRC deficit with any other country, there would be no economic advantage in shifting purchases to non-US suppliers. Moreover, given the large agricultural component where the United States is a major world supplier. China's ability to shift import sources is limited. As for machinery and equipment China's overall needs have already been cut and the share of these imports coming from the United States is concentrated in high technology goods where US firms can already outstrip the competition. 25X1

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23 September 1980

US-China Trade and Financial Relations

Trends in US-China Trade Prior to Normalization

Prior to the January 1979 normalization of relations, trade between the United States and China was characterized by erratic US exports and a slow but steady growth in US imports. The US embargo on trade with China was lifted in April 1971, permitting commercial transactions between US firms and Chinese trading corporations for the first time in two decades. The lifting of the embargo came at a propitious time for both nations. China needed grain, cotton, and soybeans in 1973-74, and the United States was the only feasible source at the time. With sales reaching $820 million in 1974, the United States temporarily became China's number-three trading partner, following Japan and Hong Kong. US agricultural exports accounted for three-fourths of total US exports to China in 1972-75. Three other deals -- for 10 Boeing aircraft, eight fertilizer plants, and 100,000 tons of aluminum -- accounted for the bulk of US nonagricultural exports through 1975. STAT

The surge, however, was short lived; China turned to other suppliers for agricultural products in 1976 and 1977, and total US sales to China dropped. During the entire period 1972-77, Peking appears to have treated the United States as a residual supplier of basic commidities -- grain, cotton, soybeans, aluminum -- buying only for short-term exigencies. China's technology purchases were

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This unclassifed memorandum was prepared by the China Division of the Office of Economic Research, National Foreign Assessment Center, in response to a Treasury Department request. Questions and comments may be addressed to STAT generally confined to areas where the United States offered unique or clearly superior products. China probably would not have incurred substantially higher costs, however, merely to avoid US goods.

STAT

In 1976 the United States registered its first trade deficit with China since 1971. US imports totaled $200 million; exports, $135 million. In first half 1976, Pullman-Kellog completed deliveries on its fertilizer plants; in the second half, US exports plummeted to $15 million. Although this downturn coincided with a sharp increase in Chinese admonishments to American businessmen that a "substantial increase in purchases" could not precede the normalization of relations, Peking may have been making a political virtue out of economic necessity. PRC imports from all hard-currency countries declined by 50 percent in second half 1976.

STAT

US exports picked up only slightly in 1977. In the fourth quarter, however, the Chinese resumed purchases of US agricultural commodities -- soybean oil and cotton. These were followed by large Chinese orders for wheat and corn in April 1978. As a result, US exports to China exceeded $800 million for the whole year with agricultural sales once again making up nearly three-quarters of the total. These sales were made at a time when other suppliers could have filled at least part of China's orders.

US purchases from China rose 60 percent in 1978, to $325 million. Clothing led all imports, jumping 150 percent to approximately $65 million. US imports of cotton fabrics, crude materials, and tin also increased sharply.

Post-Normalization Policies and Trade Trends

Foreign trade continued to flourish in 1979 and 1980 as several of the remaining obstacles to trade were removed. The Claims and Assets Agreement -- concluded in May 1979 -- settled a problem created after the outbreak of the Korean War when the PRC seized nearly $200 million worth of US property in retaliation for freezing by the United States of more than $75 million worth of Chinese assets. Prior to signing the agreement any Chinese assets brought into the United States (including ships in US harbors, aircraft, and assets in US bank accounts) were subject to seizure by holders of assets frozen in the PRC. With the United States once again in a position to carry-out direct shipping and banking relations with China the trade climate was undoubtedly enhanced.

The Sino-US trade agreement -- initialled ~~signed~~ in May 1979 and approved by Congress in January 1980 -- gives further impetus to bilateral trade. The agreement explicitly states the desire of both countries to strengthen economic ties and, more importantly, grants each country most-favored-nation status (MFN). Although the agreement is likely to have little effect on China's imports, exports to the United States will benefit from the reduced tariff rates.

Other agreements which have further improved the bilateral trade climate include the following:

- In April 1980 the US Export-Import Bank (EXIM) was given the go-ahead to finance trade with China. Although Beijing has yet to apply for any US funds, EXIM has given a preliminary commitment to finance the sale of steel mill equipment to China.
- A textile agreement reached in July 1980 clears the way for systematic, albeit constrained, growth in China's textile exports to the United States. The agreement permits larger textile shipments than currently permitted under unilateral quotas placed on China last year.
- On August 8, 1980 President Carter signed the legislation required to permit operation of the Overseas Private Investment Corporation's (OPIC's) programs in China. A major OPIC function is to guarantee US investments abroad against expropriation, inconvertibility of currency, war, insurrection, or revolution.

The improved economic environment has fostered stronger banking relations. Prior to the May 1979 signing of the claims and assets issue, fewer than 20 US banks had full correspondent relations with the Bank of China. A year later almost 50 US banks had direct ties. Commercial lending -- although still small -- has also picked up. First National Bank of Chicago extended two loans for a total of \$28 million in 1979. Earlier this year Bank of America reportedly made a \$93 million Deutchemark loan to China to finance the purchase of West German power equipment.

Bilateral trade also accelerated in the wake of the improved economic environment. China's exports worldwide rose 35 percent in 1979, sales to the US jumped nearly 85 percent to a record $595 million. Textile products -- mainly clothing -- moved up 68 percent during the year to account for almost 35 percent of total sales to the United States. Deliveries of Chinese' crude oil -- the first ever shipped to the United States -- added nearly $100 million to the value of exports and accounted for more than 15 percent of China's total exports to the United States.

Imports from the United States doubled in 1979, surpassing $1.7 billion. The rapid increase vaulted the US into position as China's second leading supplier, well behind Japan. Although grain imports were up 55 percent above year-earlier levels, they continued to account for a declining, but still major, share of imports from the United States. Purchases of US cotton and manmade fiber doubled during 1979 reaching $450 million. Textile fiber purchases stood at almost twice the level of Chinese textile exports to the United States by yearend. Imports of US iron and steel also experienced sharp gains, going from only about $1 million in 1978 to more than $165 million the following year. Other US products that made significant inroads in China's import market last year include machinery, transportation equipment, and chemicals.

This year is well on the way to being another banner year for US-China trade. During the first 5 months China's exports reached $360 million, 75 percent above year-earlier levels. Textiles and crude oil continue to account for the bulk of exports. Imports from the United States during the first 5 months of 1980 hit $1.2 billion, double the January-May 1979 level. Cotton, rather than grain, became China's leading import during the period, accounting for more than 40 percent of total purchases from the United States. Aircraft purchases were also up as Beijing took delivery on the first of three Boeing 747s ordered in 1979.

Remaining Obstacles to US-China Trade

Several obstacles -- generally much less significant than those already overcome -- may continue to inhibit US-China trade. Beijing has been pushing the United States for special tariff consideration, available only to developing countries, under the Generalized System of Preference (GSP). Although it is unclear exactly what effect GSP would have on China's exports, Beijing has made it clear that its future willingness to buy US materials depends directly on US willingness to stepped-up purchases from China. In this light, textile restrictions may also continue to be a thorny issue in future US-China trade discussions.

China's domestic problems have been the major constraint to Beijing's past plans to import Western technology. As the modernization effort gets on track, however, it is clear that China will begin a massive search for Western equipment. At that time, constraints that currently have little effect on bilateral trade may become binding. For example, Beijing continues to complain about the interest rates on US EXIM loans -- generally above 8.25 percent -- and the Bank's unwillingness to make large sums available at fixed terms. Most other major industrial countries, including Japan, France, Italy, Canada, and the United Kingdom, have broad agreements providing China with billions of dollars in government-backed credits. The credits generally carry interest rates of 7.25 - 7.5 percent and are, almost without exception, tied to major equipment purchased from the lending country. Beijing has threatened that unless the United States comes up with credit terms comparable to those offered elsewhere, purchases that would otherwise go to US firms will go to foreign businesses. Contracts for hydropower projects, where the United States reportedly has the inside track, as well as for major nonferrous metals projects, at least one of which was designed by a US firm, have been explicitly cited as dependent on low-interest US credits. Other institutional barriers to bilateral trade include US export control regulations and COCOM restrictions which limit sales of strategic items, food and drug regulations, and consumer product safety rules.

<u>US Sales Prospects</u>

Despite the remaining obstacles to US-China trade, the recently improved political climate bodes well for an expanded US share of the China market. Exports in 1980 will probably jump nearly 75 percent to more than $3 billion. Grain will probably continue to play a major, albeit reduced, role in future US sales. Shipments over the next few years will probably average 5-6 million tons per year, providing nearly one-half of China's import needs. Cotton, will also remain important at least until China's recently ordered synthetic fiber plants begin operation; at that point China's raw cotton needs become less certain.

Machinery and equipment, especially transportation and oil-drilling equipment, should become increasingly important in the future. Other major equipment orders are less certain. Engineering contracts concluded in 1978 with several US companies -- including Flour Corporation, Bethlehem Steel, and US Steel -- could have added billions of dollars to US equipment sales if the Chinese had decided to develop the projects under study. It appears now, however, that at least two of the projects -- for iron ore mining and benefication -- have fallen victim to China's shift in emphasis away from heavy industry. If the third project -- to develop of a copper mine in Jiangxi province -- receives the go-ahead it will probably be on a scaled-down version of the original design. The pace of future major machinery and equipment orders depends on Beijing's ability to implement its modernization efforts and on the ability to US firms to provide competitive bids and to line-up competitive financing.

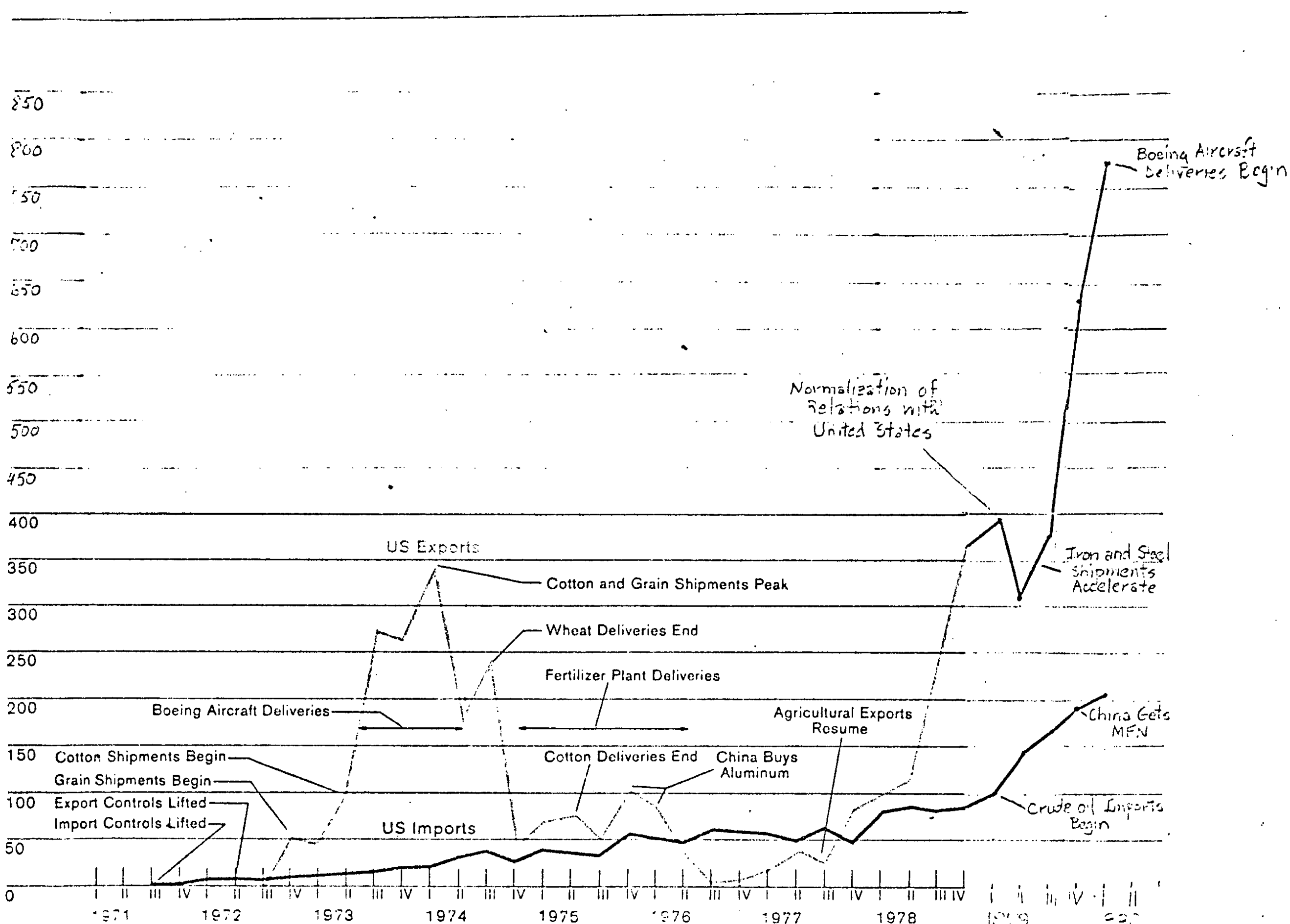
We expect that an increase in the US share of the Chinese market will come mainly at the expense of Western Europe, Australia, and Canada. The United States has already replaced the latter two countries as China's largest supplier of grain. Japan's share of China's import market has also fallen from 30 percent in 1978 to only 24 percent last year. The fall largely reflects China's cutback in steel purchases as a result of the economic readjustment. For the foreseeable future Japan will remain China's leading trade partner. Cultural and geographic proximity as well as the complementarity of the two economies ensures Japan a solid share of the future market. Japan's successes in the China market sometimes benefits the United States; in many cases US firms hold the licenses for the technologies involved in Japanese equipment sales and thus share in the revenues.

Chinese Export Prospects

China presumably considers the possibility of increased sales to the United States as a major benefit of the normalization process. In 1978, even before normalization took effect, Chinese sales to the United States jumped by 60 percent, to $325 million. The United States thus surpassed West Germany, Singapore, and Romania as a market for Chinese exports, and moved into its present position behind Japan and Hong Kong. This year sales to the United States should surpsss $1 billion. Even so, the United States, which takes about 15 percent of total world exports, still accounts for only 4 percent of Chinese exports. Imports from China represent only 0.3 percent of US imports.

The recently concluded bilateral textile treaty provides considerable potential for increasing textile and clothing exports to the United States. Oil exports to the United States have only small potential due to Chinese supply constraints and the ample West Coast oil supply. As with Chinese exports in general, strong export growth in the United States in the future will depend on China's ability to break into markets for higher priced consumer products, including clothing and consumer electronics. Chinese success in building dedicated export plants to provide ample supplies of quality products could result in substantial increases in shipments to the US market over the next few years.

Highlights of US-China Trade[1]
Million US $



1. Data are from US Department of Commerce and show exports on an f.a.s. and imports on an f.o.b. basis.

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CHINA: EXPORTS TO UNITED STATES 1/

Million US$

COMMODITY	1978 I	1978 II	1978 III	1978 IV	1979 I	1979 II	1979 III	1979 IV	1980 I	Annual 1977	Annual 1978	Annual 1979
Total Exports	79.4	86.7	80.8	77.2	100.8	144.8	165.3	180.5	204.7		324.1	591.4
Agricultural Goods	16.6	22.2	17.0	14.3	17.9	26.3	23.0	23.3	27.2		70.2	90.4
Shellfish	.1	.2	.1	.4	3.7	4.4	5.8	1.7	.5		.8	15.6
Nuts	2.1	.5	2.7	2.4	1.2	1.7	2.9	2.1	.3		7.7	7.8
Sugar & Sirups	.0	.1	.1	.1	.5	1.3	2.0	2.9	2.1		.3	6.7
Tea	.6	1.2	1.2	1.8	1.5	1.9	1.9	2.4	3.5		4.8	7.7
Spices	.6	.8	1.0	.6	1.6	1.3	.6	.7	.8		2.9	4.1
Feather, Downs	8.2	14.2	7.2	3.7	3.5	6.6	4.7	5.5	10.5		33.4	20.3
Wood & Paper Products	4.8	5.3	5.2	5.4	6.5	6.6	6.1	8.7	9.6		20.7	27.9
Bamboo Products	4.3	4.7	4.5	4.8	5.8	5.8	5.3	7.7	8.4		18.3	24.6
Textile Fiber & Prod	25.4	32.6	34.7	26.9	35.6	39.4	73.1	53.3	61.3		119.6	201.5
Wool, Animal Hair	1.7	1.6	.5	.7	1.5	.3	.8	1.7	1.5		4.5	4.3
Silk Fiber & Yarn	.6	.7	1.7	1.7	1.3	1.6	3.0	2.1	1.1		4.7	8.0
Cotton Fabrics	9.4	11.3	8.4	8.8	7.0	4.3	7.1	6.1	8.2		38.0	24.5
Silk Fabrics	.3	.2	.7	.3	.6	.5	.4	.7	1.0		1.5	2.2
Rugs & Carpets	2.8	2.4	2.5	2.8	4.8	3.4	5.1	3.9	7.6		10.5	17.2
Clothes	8.8	13.9	19.5	10.6	18.4	27.5	53.3	34.2	36.0		52.8	133.4
Chemicals	5.3	4.2	5.1	7.8	6.3	8.6	13.8	19.9	23.4		22.5	48.7
Inorganic	.8	.6	1.1	1.0	1.0	1.7	5.2	10.8	13.0		3.6	18.7
Essential Oils	1.9	1.4	1.0	2.7	1.2	1.5	1.3	2.0	2.3		7.0	5.9
Petroleum					10.6	32.1	16.0	37.7	36.4			96.5
Crude					10.6	32.1	13.0	16.0	18.8			71.8
Products							3.0	21.7	17.5			24.7
Nonmetallic Minerals	1.4	1.3	1.3	1.5	1.3	3.4	2.5	2.4	3.9		5.4	9.6
Metals & Metal Prod	13.7	5.8	5.9	6.5	5.8	6.8	7.2	11.0	17.5		32.0	30.7
Ores	1.4	1.6	.8	2.6	1.7	2.9	2.4	4.5	3.2		6.4	11.5
Tin	10.0	1.8	3.0	.7	.5	.4		1.8	3.6		15.5	2.7
Machinery & Transp. Eq.	.1	.2	.1	.1	.2	.3	.4	.4	.4		.5	1.3
Miscellaneous	12.1	15.0	11.5	14.6	16.6	21.3	23.2	23.8	25.1		53.3	85.0
Footwear	.9	.7	.8	1.0	1.8	3.6	6.2	3.8	3.8		3.4	15.3
Headwear	1.5	.4	1.0	1.5	1.3	1.1	1.3	1.9	2.3		4.3	5.6
Gloves	1.8	1.9	2.6	2.5	4.1	4.1	4.8	4.1	4.3		8.8	17.2
Fireworks	2.9	4.0	1.2	3.9	3.8	6.3	2.4	3.1	3.9		12.1	15.6
Antiques	2.4	4.1	2.2	2.9	3.4	3.0	3.6	3.6	4.7		11.6	13.6

1/ Data is from U.S. Customs Bureau and is slightly different from the IMF data used in Tables 1 - 4. U.S. imports are on an f.a.s. basis - very close to f.o.b. - hence do not need an adjustment to reflect Chinese exports f.o.b. Categories are based on the TSUSA nomenclature which the U.S. uses. SITC breakdown will be available annually.

CHINA: IMPORTS FROM UNITED STATES 1/

Million US$

COMMODITY	1978				1979				1980	ANNUAL		
	I	II	III	IV	I	II	III	IV	I	1977 2/	1978	1979
Total Imports............	97.5	113.6	230.3	379.6	395.3	314.4	376.7	637.6	774.8		821.0	1,724.0
Agricultural Goods......	.0	54.9	101.3	259.7	188.0	113.6	134.5	205.9	229.1		415.9	642.0
Corn.................				111.7	109.7	65.8	4.4	88.7	73.4		111.7	268.5
Wheat................		30.9	87.0	132.3	49.3	13.0	129.3	22.4	55.0		250.2	214.1
Soybeans.............		17.5	8.6	15.3	28.0	30.3		84.3	85.0		41.4	142.6
Wood & Paper Products..	.7	.0	4.0	.2	3.8	.2	2.6	2.1	4.8		4.9	8.6
Printed Matter.......	.1	.0	.1	.2	.1	.1	.6	.3	.8		.4	1.2
Textile Fiber & Prod...	66.4	34.7	71.9	34.1	86.6	73.7	68.3	224.7	314.1		207.2	453.3
Cotton...............	54.9	24.9	53.5	24.0	68.2	64.8	36.5	187.5	275.3		157.3	357.0
Manmade Fiber........	11.5	9.6	18.4	8.3	16.0	7.9	30.7	35.4	35.6		47.8	90.0
Chemicals..............	8.3	7.9	24.6	20.3	38.2	18.7	23.1	46.8	83.7		61.1	126.8
Inorganic............	.4	.1	.8	.8	4.1	2.4	4.6	2.6	4.2		2.1	13.7
Synthetic Resins.....	1.0	.0	.9	.0	5.3	3.8	8.8	12.7	18.9		2.0	30.6
Fertilizer...........	1.8	5.6	19.8	11.5	12.5	8.0	1.9	22.2	24.3		38.7	44.6
Pesticides...........	2.4	.8	.9	6.1	10.8	2.3	1.4	4.9	20.9		10.3	19.4
Nonmetallic Minerals...	.0	.0	.0	1.7	.1	.3	.2	.4	.9		1.7	1.0
Metals & Metal Prod....	3.9	.8	4.7	12.3	19.6	39.1	84.3	59.1	22.0		21.6	202.2
Iron & Steel.........	.1	.2	.8	.2	8.6	23.7	76.7	53.9	4.3		1.3	163.0
Tools................	3.6	.5	3.7	6.0	5.8	7.6	2.8	2.3	2.5		13.7	18.6
Machinery..............	13.9	10.5	15.5	36.8	37.1	37.3	34.5	57.0	48.0		76.6	165.8
Earth Moving.........	1.4	1.0	2.8	28.5	18.7	21.7	14.1	38.7	20.8		33.7	93.2
Material Handling....	.0		.0		1.1	2.4	1.2	.3	.7		.0	5.0
Machine Tools........	3.0	1.2	.8	1.0	.4	1.0	2.9	.7	.1		6.0	4.9
Data Processing......	.0	.5	.2	.5	1.0	.8	2.0	7.0	11.5		1.1	10.9
Communications.......	.4	.1	.3	1.0	.8	3.1	2.2	2.0	1.1		1.8	8.1
Transportation Equip...	3.1	3.2	2.1	9.0	13.8	17.7	13.8	19.0	57.2		17.4	64.3
Motor Vehicles.......	3.1	3.1	2.1	8.0	11.4	14.5	13.4	12.2	2.6		16.4	51.6
Aircraft.............	.0	.0	.0	.3	.0	.5	.4	6.8	54.6		.4	7.7
Miscellaneous..........	1.2	1.5	6.2	5.6	8.2	13.8	15.3	22.7	15.1		14.5	59.9
Survey, Navigation Eq	.0	.4	1.5	.2	2.8	4.3	8.1	9.2	7.2		2.1	24.4
Measuring, Test Eq...	.8	.7	4.3	4.0	3.8	6.5	5.2	8.7	4.9		9.8	24.2
Movies...............	.0	.0	.0	.7	.5	.8	.4	1.3	.1		.8	2.9

1/ Data is from U.S. Customs Bureau and is slightly different from the IMF data used in Table 1 - 4. It, moreover, does not include wheat transhipments through Canada which we have added to the IMF data. Categories are based on the U.S. Schedule B nomenclature. SITC will be available annually.

2/ Due to change in U.S. trade nomenclature, 1977 data on Schedule B basis is not avaiable.

BLUMENTHAL BRIEFING BOOK
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Sino-American Economic Relations

At an 18 December press conference in Hong Kong, China's Minister of Foreign Trade, Li Chiang, stated, "China's policy in reaching trade agreements gives priority to countries having diplomatic relations with China when similar terms are offered. Now the United States and China have agreed to establish diplomatic relations. This will make a difference in trade between the two countries." Later, at a reception for businessmen, Li said, "Trade between China and the United States will definitely increase sharply." We believe Li's statement, although it overemphasizes the impact of normalization, is an accurate assessment of the future trend in US-China trade.

Past and Present Bilateral Economic Relations

Trade between the United States and China has been characterized by erratic U.S. exports and a slow but steady growth in U.S. imports (see figure). The U.S. embargo on trade with China was lifted in April 1971, permitting commercial transactions between U.S. firms and Chinese trading corporations for the first time in two decades. The opening of economic relations came at a fortuitous time. China needed grain, cotton, and soybeans in 1973-74, and the United States was the only feasible source at the time. With sales peaking in 1974 at $820 million, the United States quickly became China's number-three trading partner, following Japan and Hong Kong. Agricultural exports, which accounted for three-fourths of total US exports to China in 1972-75, were rapidly phased out with China's import needs being met by the traditional suppliers. Three other deals --for 10 Boeing aircraft, eight fertilizer plants, and 100,000 tons of aluminum -- accounted for the bulk of US nonagricultural exports through 1975. While it is unlikely that the Chinese were willing to incur substantially higher costs to avoid US goods, Peking viewed the United States as a residual supplier of basic commodities -- grain, cotton, soybeans, aluminum -- buying only for short term exigencies.

In 1976 the United States registered its first trade deficit with China since 1971. US imports totaled $201 million; exports, $135 million. In the first half of 1976 Pullman-Kellogg completed deliveries on its fertilizer plants, and in the second half US exports plummeted to $15 million. Although this downturn coincided with a sharp increase in Chinese admonishments to American businessmen that a "substantial increase in purchases" could not precede the normalization of relations, Peking may have been making a political virtue out of economic necessity. PRC imports from all hard currency countries declined by 50 percent in the second half of 1976.

U.S. exports picked up only slightly in 1977. In the fourth quarther, however, the Chinese resumed purchases of US agricultural commodities--soybean oil and cotton. These were followed by large Chinese orders for wheat and corn in April 1978. As a result, last year US exports to China exceeded $800 million, once again with agricultural sales comprising nearly three-quarters of the total. Strangely, these sales were made at a time when other suppliers could have filled at least part of China's orders. In part, the Chinese may have made these purchases in order to encourage U.S. farmers' support for normalization.

U.S. purchases from China, stagnant in 1977, rose 60 percent in 1978 to $324 million. Clothing led all imports jumping 150 percent to approximately $65 million. U.S. imports of cotton fabrics, crude materials, and tin also increased sharply.

Current Impediments to Economic Relations

Lack of diplomatic relations has been only one of several political obstacles to the expansion of U.S.-China trade. Lack of most-favored-nation tariff treatment for Chinese exports renders some Chinese commodities non-competitive and forces the American businessman and consumer to pay more for others. Lack of Export-Import Bank financing puts U.S. firms at a disadvantage in competing for major sales with firms in Japan and Western Europe. COCOM restrictions and other strategic trade controls prevent the sales of items with military applications. Finally, the related issued of blocked Chinese assets and private U.S. claims, stemming from actions taken at the beginning of the Korean War, prevent direct shipping and airline connections, direct banking relations, and the exchange of trade exhibitions, owing to the risk of attachment of Chinese assets to satisfy claims. Presumably Peking not only wants, but also feels entitled to a resolution of these problems as part of the normalization process, and Peking may continue to use the promise of increased trade as a lever to push for a settlement in their favor.

Future U.S. Sales Prospects

Despite the remaining obstacles to US-China trade, the recently improved political climate bodes well for an expanded US share of the China market. Grain will probably continue to play a major, albeit reduced, role in future

US sales. Shipments over the next few years will probably average 5-6 million tons per year -- providing nearly one half of China's import needs. Cotton, which accounted for roughly one-fifth of US sales in 1978, will also remain important at least until China's recently ordered synthetic fiber plants begin operation; at that point China's raw cotton needs become less certain.

Machinery and equipment, especially transportation and oil drilling equipment should become increasingly important in the future. Recent engineering contracts with several US companies, including Fluor Corp., Bethlehem Steel and US Steel, could add hundreds of millions of dollars to US equipment sales if the Chinese decide to develop the projects under study.

We expect that an increase in the U.S. share of the Chinese market will come mainly at the expense of Western Europe, Australia, and Canada. The US has already replaced the latter two countries as China's largest supplier of grain. Japan's 30 percent share of China's import market may fall somewhat as a result of the recent appreciation of the yen but for the foreseeable future Japan will remain China's leading trade partner. Cultural and geographic proximity as well as the complementarity of the two economies ensures Japan a solid share of the future market. Japan's fortunes in the China market are not without benefits to the United States. In many cases US firms hold the licenses for the technologies involved in Japanese equipment sales and hence receive a share of the revenues.

Chinese Exports to the United States

We believe that if China is serious about rapidly increasing export earnings to meet import needs, Peking must be looking to the U.S. as a prime market for increasing sales. Given the multiple suppliers of most of China's imports, China may consider increased sales to the U.S. as important a benefit of the normalization process as easier access to U.S. technology.

Chinese sales to the U.S. jumped by 60 percent to $324 million in 1978. The U.S. thus surpassed West Germany, Singapore, and Romania as a market for Chinese exports, but was still a distant third behind Japan and Hong Kong. The United States still, however, takes an atypically small share of Chinese exports. The U.S., which takes about 15 percent of total world exports, accounts for only three percent of Chinese exports. Imports from China, moreover, are only two tenths of one percent of total U.S. imports.

Two key issues concerning potential Chinese export increases are the MFN and frozen assets questions. Non tariff barriers such as quotas on Chinese textiles will also arise as U.S. imports increase. Recent studies of the impact of lack of MFN status have indicated that Chinese exports to the U.S., might be approximately 30 percent higher than actual levels.* The studies argue, however, that this impact will rise as China attempts to export higher value added products. The frozen assets problem will also have to be settled if China is going to improve its marketing capability - through trade fairs and the like - in the U.S.

Table____ includes a list of the most important U.S. imports in 1978. Cotton fabric imports, the largest item, accounted for five percent of total U.S. imports of that commodity in 1977 rising to ten percent in 1978. Following sharp increases in 1976 some U.S. concern for the need for quotas was expressed. The problem was temporarily resolved by the 1977 decline in Chinese fabric exports but may rise again if the 1978 increase continues. United States clothing imports of all types from China totalled about $65 million in 1978, 2 1/2 times 1977 imports but still accounting for only 2 percent of U.S. clothing imports.

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* See Lincoln, Kilpatrick and Raffel, Teal, McQueen in <u>Chinese Economy Post Mao</u> JEC 1978.

Among other important items, Chinese exports of feathers and downs accounted for 29 percent of U.S. imports in 1977, basketwork approximately 10 percent of U.S. imports, and fireworks approximately half of U.S. imports. China held only 1 percent of U.S. tin imports in 1977 increasing to 3 percent in 1978.

Considerable potential exists for increasing textile and clothing exports to the U.S. if MFN and quota arrangements can be made. The Chinese are, however, at this point hesitant to discuss quotas because of what they perceive as a US policy to set quotas based on past imports giving them an unfair small share of the market. Oil exports - the first contract for 500,000 tons was signed in late 1978 - holds fairly limited potential due to Chinese supply constraints and the ample West Coast oil supply. It appears that as with Chinese exports in general, strong export growth to the United States in the future will depend on China's ability to break into higher value added goods such as finished consumer products. Chinese success is building plants to provide these goods could mean a very large increase in U.S. imports from China by the end of the current plan.

Major Chinese Exports to U.S.

Million $

	1976	1977	1978
Total	202	203	324
Cotton fabrics	32	17	37
Feathers	14	19	26
Tin	13	4	16
Women's slacks	3	5	16
Basketwork	10	11	k5
Fireworks	6	10	13
Antiques	10	8	12
Carpets	4	7	10
Men's sweaters	2	6	10
Men's trousers	NA	NA	9